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# Need for Attribution— Second Circuit Affirms that Plaintiffs Need to Show Reliance on Secondary Players' Own Statements

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In *Pacific Investment Management Co. LLC v. Mayer Brown LLP*,[1] the Second Circuit held that a secondary actor can be liable in a private action under § 10(b) of the Securities Exchange Act of 1934 (the "Exchange Act") and Rule 10b-5(b),[2] only for false statements attributed to the secondary-actor at the time the statement is disseminated. The court reasoned that absent attribution, plaintiffs could not show that they relied on defendants' own false statements, and creating those statements amounted to mere aiding and abetting, which, under *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*[3] cannot form the basis of a securities fraud claim. The court also held that claims under Rule 10b-5(a) & (c) against an undisclosed participant in a scheme to defraud investors are barred by the Supreme Court's holding in *Stoneridge Investment Partners, LLC v. Scientific-Atlanta, Inc.*[4]

Refco, Inc. was a large brokerage and clearing firm. For 20 years, Joseph Collins served as Refco, Inc.'s, outside counsel, including 10 years as a partner at Mayer Brown LLP. After suffering significant losses in the late 1990s, Refco and Mayer Brown manufactured a series of sham loan transactions in order to conceal the losses. Ultimately, in 2005, Refco declared bankruptcy.

CONTINUED ON PAGE 3

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Plaintiffs—investors in Refco securities—brought suit under § 10(b) alleging that between 2000 and 2005, Mayer Brown and Collins participated in 17 sham transactions. Specifically, Mayer Brown and Collins negotiated the terms of the loans, drafted and revised loan documents, transmitted the documents to the participants, and retained custody of, and distributed executed copies. Plaintiffs also alleged that Mayer Brown was responsible for false statements that appeared in three Refco documents: (1) an offering memorandum for an unregistered bond offering in July 2004; (2) a registration statement for a later bond offering; and (3) a registration statement for the initial public offering of common stock in August 2005. The documents were false or misleading because they failed to disclose Refco's true financial condition, which was concealed by the sham loan transactions. Although two of the documents listed Mayer Brown as counsel, none attributed any specific information to Mayer Brown or Collins.

The district court (Judge Gerard E. Lynch, since elevated to the Second Circuit) dismissed plaintiffs' claims against Mayer Brown and Collins. In deciding *In re Refco, Inc. Sec. Litig.*,[5] the district court held that, because no statements in Refco's public documents were attributed to Mayer Brown or Collins, at most plaintiffs had alleged conduct akin to aiding and abetting—for which, under *Central Bank*, there is no private right of action under securities laws. The district court also dismissed plaintiffs' Rule 10b-5(a) and (c) claims for "scheme liability" as foreclosed by the Supreme Court's decision in *Stoneridge*.[6]

On appeal, both the plaintiffs and the Securities & Exchange Commission, writing as *amicus curiae*, argued that that a defendant can be liable for *creating* a false statement that investors rely on, regardless of whether that statement is attributed to the defendant at the time of dissemination. Defendants responded that attorneys who participate in the drafting of false statements could not be liable for a primary violation of Rule 10b-5(b) absent explicit attribution at the time of dissemination.

The Second Circuit affirmed. The court remarked that there were two lines of cases discussing secondary actors' liability. In *Wright v. Ernst & Young LLP*,[7] the court held that "a secondary actor cannot incur primary liability under [Rule 10b-5] for a statement not attributed to that actor at the time of its dissemination." *Wright* involved claims that an accounting firm had orally approved a corporation's false and misleading financial statements, which were subsequently disseminated to the public. In *Lattanzio v. Deloitte & Touche LLP*,[8] the court reiterated the attribution requirement for secondary actors' liability. In contrast, in *In re Scholastic Corp. Securities Litigation*,[9] the court held that a corporate officer who was involved in the drafting, producing, reviewing, and disseminating of false and misleading statements may be liable for misrepresentations made by the corporation, even though none of the statements were specifically attributed to him when disseminated.[10]

## Rejecting the 'Creator' Standard

In *Pacific Investment*, the Second Circuit firmly adopted the attribution requirement and rejected the "creator" standard urged by the plaintiffs and the SEC. Noting that "[a]ttribution is necessary to show reliance," the court reasoned that the attribution requirement was more consistent with the Supreme Court's emphasis on the element of reliance in *Stoneridge*. The court suggested that an attribution requirement was preferable because it established a "bright line" rule, as opposed to the "substantial participation" rule stated in *Wright*. The court explicitly declined to reconcile *Wright* and *Scholastic*, stating in a footnote that, because the case did not involve claims against corporate insiders, it would "intimate no view on whether attribution is required for such claims or whether *Scholastic* can be meaningfully distinguished from *Wright* and *Lattanzio*."

 

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The court also affirmed the dismissal of plaintiffs' Rule 10b-5(a) and (c) claims on the ground that the Supreme Court's decision in *Stoneridge* foreclosed plaintiffs' theory of "scheme liability." The court held that under *Stoneridge*, a claim for scheme liability will not lie unless the plaintiff alleges reliance on the defendants' own deceptive conduct. Because the plaintiffs admitted that at the time of their purchases they were "unaware of defendants' deceptive conduct or 'scheme,'" the court reasoned, they could not show reliance. The court expressly rejected the argument that reliance occurs when a secondary actor's deceptive course of conduct is communicated to the public through a company's financial statement. The court acknowledged that under its interpretation of *Stoneridge*, "it is somewhat unclear how the deceptive conduct of a secondary actor could be communicated to the public and yet remain 'deceptive.'"

In a concurring opinion, Judge Barrington Parker invited a petition for rehearing *en banc*. "In light of the importance of the existence, *vel non*, of an attribution requirement to the securities laws, the bar, and the securities industry, this case could provide our full Court, as well as, perhaps, the Supreme Court, with an opportunity to clarify the law in this area."

**NOTES**

1. *Pacific Inv. Management Co. LLC v. Mayer Brown LLP,* Fed. Sec. L. Rep. (CCH) P 95722, 2010 WL 1659230 (2d Cir. 2010).
2. The Securities Exchange Act of 1934, 15 U.S.C.A. § 78j(b); and Rule 10b-5(b), 17 C.F.R. § 240.10b-5, respectively.
3. *Central Bank of Denver, N.A. v. First Interstate Bank of Denver, N.A.*, 511 U.S. 164, 114 S. Ct. 1439, 128 L. Ed. 2d 119, Fed. Sec. L. Rep. (CCH) P 98178 (1994).
4. *Stoneridge Inv. Partners, LLC v. Scientific-Atlanta*, 552 U.S. 148, 128 S. Ct. 761, 169 L. Ed. 2d 627, Fed. Sec. L. Rep. (CCH) P 94556 (2008).
5. *In re Refco, Inc. Securities Litigation*, 609 F. Supp. 2d 304, 311-314 (S.D. N.Y. 2009), aff'd, Fed. Sec. L. Rep. (CCH) P 95722, 2010 WL 1659230 (2d Cir. 2010).
6. See *Refco*, 609 F. Supp. 2d at 314-319.
7. *Wright v. Ernst & Young LLP*, 152 F.3d 169, 175, Fed. Sec. L. Rep. (CCH) P 90266 (2d Cir. 1998).
8. *Lattanzio v. Deloitte & Touche LLP*, 476 F.3d 147, Fed. Sec. L. Rep. (CCH) P 94150 (2d Cir. 2007).
9. *In re Scholastic Corp. Securities Litigation*, 252 F.3d 63, Fed. Sec. L. Rep. (CCH) P 91455 (2d Cir. 2001).
10. *Scholastic*, 252 F.3d at 75-76.